WEFA Soviet Trade Forecasts

The 24 January Financial Times article calling for a major boost in Soviet trade with the West is based on a Current Analysis issued by Wharton Econometrics in late December. Although WEFA revised this projection on 7 January, the basic forecast was not changed. In the projection, WEFA calls for Soviet exports to the developed West in 1983 to grow by 3 percent and imports to grow by 18 percent (both in nominal terms).

In dollar terms, the 3 percent export increase translates into a not too unreasonable $600 million increase in Soviet exports, while the 18 percent jump in imports is equal to a $4.7 billion increase. With respect to exports, one-half the increase is to come from stepped up sales of non-food raw materials. WEFA anticipates that energy sales will increase marginally--by $100 million, all due to a 0.5 percent oil price rise. WEFA attributes most of the increase in imports to stepped purchases of investment goods for energy development, particularly the pipeline.

WEFA's trade forecasts are much more optimistic than we are projecting in the Office of Soviet Analysis. With respect to export growth, much will hinge on oil pricing developments during the year. In light of OPEC's current problems we expect energy prices to fall again in 1983. It should be noted that WEFA's forecast was formulated before the disagreements within OPEC on production and pricing came to a head. As for imports, we agree that purchases of energy equipment (especially for the export pipeline) will increase in 1983. Our forecast of the increase in total imports, however, is smaller, perhaps rising by only $3 billion.

In the longer term--through 1987--WEFA forecasts a substantial and sustained growth in trade with the developed West. WEFA forecasts exports to grow (in nominal terms) at a rate of 10 percent a year and imports to grow at a rate of 12 percent a year during 1983-87. These projections are based on a combination of optimistic assumptions regarding Western demand for Soviet exports, energy price trends, and Soviet ability to expand non-energy exports while limiting the fall in real energy exports to 1 percent per annum. In addition, WEFA expects that Andropov will rely heavily on imports to boost economic growth and consequently projects real import growth forward at a nearly 6 percent annual rate. Machinery and equipment is projected to grow especially fast, at an 8.1 percent annual rate.

We do not believe that growth rates for either Soviet exports or imports will approach those forecast by WEFA. Crucial to any projections on trade are the assumptions made on energy prices. Although energy price trends are extremely difficult to predict, the present situation in the energy market indicates the

possibility that oil prices may be soft for a while. In any event, we are skeptical that the rapid growth in oil prices which occurred during the 1970s is likely to reoccur in the 1980s. Consequently we see little possibility of increased earnings from energy exports. Rather, Moscow may be doing well if foreign exchange earnings do not fall too steeply due to an erosion in export volume.

We are even less optimistic on non-energy export trends. In contrast to WEFA--which is projecting relatively rapid growth in non-energy exports--we do not expect these exports to grow by much more than one percent per annum in real terms. Barring a quick Western economic recovery, Soviet exports of non-energy raw materials will be constrained by a combination of increasingly severe domestic production problems and weak Western demand. Because Soviet machinery and equipment has generally been uncompetitive in the West, increases in these exports at the rate projected by WEFA--8.8 percent in real terms--appear to be especially unrealistic.

The trade trends forecast by WEFA calls for imports to grow 2-3 percent a year faster than exports. Financing needed to cover the gap in trade will cause hard currency debt to double between 1982 and 1987. While we agree that a 2-3 percent spread between imports and exports is reasonable, we are not convinced by WEFA's assertion that the build up in debt is managable. Underlying Wharton's analysis is an argument that debt service obligations can be met through the increase in exports they are projecting. If, as we believe, exports stagnate, even an annual import growth rate substantially lower than 6 percent projected by WEFA is likely to push debt to a level unacceptable to the Soviet leadership.